

Support to the Contract Management Unit of the Greater Johannesburg Metro Council

Final Draft Report

Functional Analysis and Implementation Strategy

for City of Johannesburg Contract Management Unit

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REPORT ON FUNCTIONAL ANALYSIS AND IMPLEMENTATION STRATEGY FOR CMU

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FUNCTIONAL ANALYSIS AND IMPLEMENTATION STRATEGY FOR CMU

1. EXECUTIVE SUMMARY

1.1 Introduction

The Johannesburg City Council has designed and implemented a wide range of reforms designed to improve the financial performance, efficiency and accountability of public service delivery. A key component of this reform was the transformation of twelve former municipal service departments and agencies into utilities, agencies and corporatised entities (UACs) under the Companies Act. A Contract Management Unit (CMU) was created to negotiate Service Delivery Agreements (SDA's) under which the UAC's provide either public services to the residents of the City, or support services to the City Administration. The CMU is also charged with monitoring the performance of the service providers and their compliance with the SDA's.

The Council requested specialist advisory inputs to ensure that international best practices were being employed by the CMU. PADCO was selected by the United States Agency for International Development (USAID) to provide Technical Assistance to the CMU for that specific purpose. In addition, The World Bank, with funding from the Cities Alliance, also contributed funding and expert assistance to the Advisory Team.

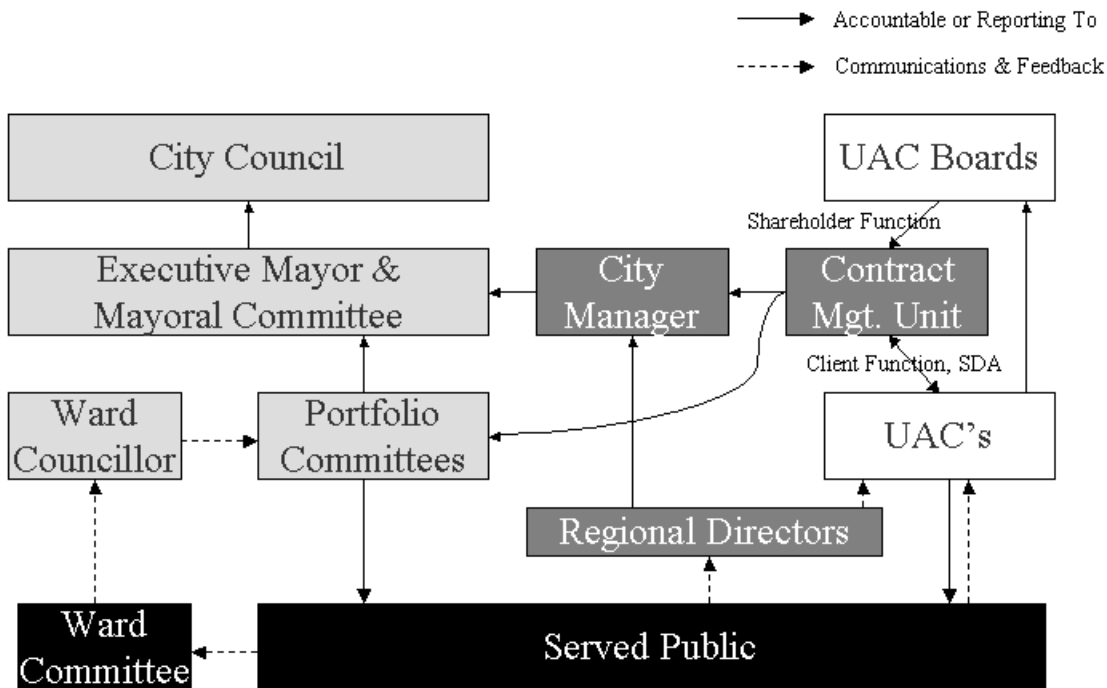
In carrying out its analysis, the PADCO Advisory Team interviewed a variety of stakeholders. These included the entire staff of the CMU, three of the four Portfolio Committee Chairpersons of the City Council, and the Managing Directors or senior staff of all of the UAC's. In addition, informational meetings were conducted with consulting advisors under contract to the CMU; representatives of the National Department of Finance, and the Executive Director of Finance for the City.

The Analysis Phase made it clear to the Advisory Team members, that the issues were larger than merely the form, function, and staffing of the CMU. More basic questions were being raised as to the role, responsibility and authority of the CMU, and the channels of reporting for the UAC's. Thus, the Advisory Team agreed to identify the key roles to be played in contracting and supervising the UAC's, and recommend how these roles might be allocated among the Council, City Management, and the CMU, in light of existing law as well as international best practice. The intent of this broader approach was to provide an objective set of recommendations, as they relate to ensuring and protecting the public interest in the delivery of public services.

1.2 The Johannesburg Model - Fundamental Issues

Based on the analysis, a generalized depiction of relationships under the Johannesburg model was drawn up, as shown in the following diagram, "Johannesburg Today".

Johannesburg Today



The Advisory Team perceived a lack of clarity in some of the roles depicted, particularly between the client and shareholder roles, and identified a number of issues, as described below.

- The UAC's have now been formed as corporations. As such, a corporation needs to have its strategy agreed with its shareholder.

Issue: Long-term corporate strategies do not appear to be in place, at least from reading the current business plans.

- City Council is the shareholder of the UAC's. As such Council has interests in setting the strategic course for each UAC, in ensuring preservation of capital and protection of the asset base, and in obtaining a return on the invested capital.

Issue: Portfolio Committees seem to have this role, while also being held responsible for the client role described below.

- Municipal government represents the served public as client of the UAC's. As such, government is the counterpart to the SDA's, to ensure that service standards are met at the least cost to the served public.

Issue: Serving the public is the primary focus of the interest of Portfolio Committees, rather than the shareholder role described above.

- The CMU is a unit of the City, and is thus an instrument of government. Hence the CMU's primary role is to ensure compliance with SDA's, on behalf of government.

However, a vacuum has been created in addressing shareholder concerns with UAC's, and so as the primary interface between Council and the UAC's, CMU is filling that need.

Issue: UAC's perceive CMU as wearing not only the client hat, but also the shareholder hat, because CMU attends Board meetings and advises on Business Plans. Correspondingly, Portfolio Committees perceive CMU as representing UAC's.

- The model has not yet been fully formed as to the aspects of price setting. There are three phases of price setting: tariff policy, tariff methodology, and tariff formulation through negotiation. In the model, setting tariff policy will not be the role of CMU, but that role is not yet fulfilled by others.

Issue: In the absence of a tariff policy, CMU may be called upon to act beyond its authority to determine policy. Therefore, the UAC's perceive the CMU as wearing a third hat, that of a regulator.

1.3 Diversity of UACs Requires Different Contract Management Approaches

The UACs are not a homogenous group as regards their economic characteristics and market conditions. As a result, some require primarily contract management while others require more policy input and regulation (to pursue social objectives and compensate for market failures). For others, the City is not really a client, but only the shareholder (e.g. Civic Theatre). To take full advantage of the benefits of corporatisation and rationalise shareholder, client and regulatory functions, it is essential to recognise the differences. They can best be understood when the UAC's are grouped with regard to the following parameters:

- Whether the services are delivered directly to the residents of the city or as support services to the City Administration;
- Whether the services are monopolistic, natural or *de facto*, or are subject to competition;
- Whether the services provided to the residents are private goods for which users pay on the basis of consumption, or public goods, which are paid for out of general revenues, or for which users pay only nominal fees.

Essential services for which users pay (especially monopolies like water) require contract management and tariff setting process. Public services without user fees and administrative support services require contract management (as a client). Competitive private goods require least oversight (primarily shareholder oversight).

1.4 Responsibility of the Shareholder to Define Corporate Strategy

The Advisory Team's understanding is that today's status is the final state for UAC's. Therefore, the Advisory Team suggests that Council (as shareholder) should now determine a long-term strategy for each UAC. One key element of strategy will be financial, whether the UAC is called upon to be a profitable, growing public sector enterprise, a breakeven enterprise, or a subsidised loss-making enterprise. Another will be whether the enterprise is being positioned for a future commercial direction.

The Advisory Team recommends that City Council recognise its shareholder responsibility, and establish or appoint a political organisation to fulfil the role. This political organization (or individual) would take a long-term view and would approve members to UAC's Boards of Directors, establish strategy for each UAC, and provide policy direction to Boards of Directors. Correspondingly, this organisation would be supported by an arm of the City Administration, such as an "office of shareholder services".

1.5 Municipal Government's Duty as Service Authority/Client

The Advisory Team observed that Johannesburg has made substantial progress in implementing the new model by establishing SDA's, and that Portfolio Committees and the CMU are actively pursuing their responsibilities as client under the SDA's. These responsibilities include defining level and quality of services, negotiating Key Performance Indicators, and monitoring performance. The next step, often the most difficult one in such relationships, will be to negotiate the tariff or budget subsidy. This step has been delayed until the Finance Department is able to determine opening balance sheets for each UAC, which is expected very soon.

The Advisory Team suggests that CMU be the principal instrument of Municipal Government responsible for representing the Client's interests. As its name implies, primarily responsible for management of contracts for services, the CMU:

- Translates policy directives on public services from Council (Executive Mayor and Portfolio Committee) to service provider;
- Negotiates service level, quality and price with the service provider;
- Develops SDA terms with the service provider;
- Monitors performance and enforces compliance based on SDA's.

1.6 Clarifying the Role of CMU and Its Relationships

In order to clarify the CMU's role, it is best to first define the role of the UAC's. The management of each UAC is accountable to its Board of Directors, and UAC management prepares a business plan for the Board. The Board is accountable to City Council (through the appropriate committee or individual designated as shareholder). UAC management reports to CMU, according to agreed contract monitoring procedures.

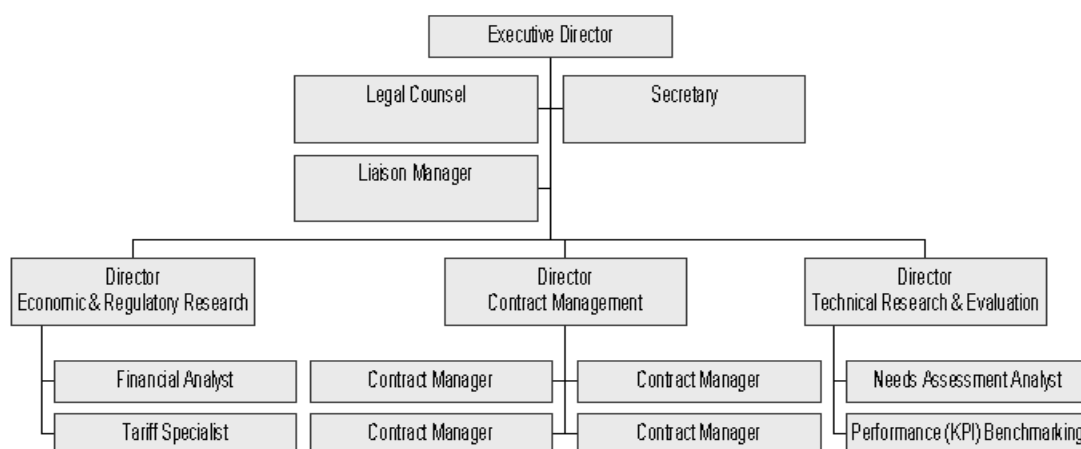
The Advisory Team sees the role of CMU as contract manager in a negotiated procurement (as regards most UAC's), and in some cases competitive procurements (such as for City support services). To the UAC's, the CMU is also acting as an intermediary in the regulatory process, since the City assumes the role of authority in several instances. In its role, the CMU needs to be focused on contract compliance and performance monitoring, rather than business monitoring. Because of its core competence, the CMU will need clear criteria to avoid becoming the City's purchasing agent for all manner of commodities (procurement creep).

The Advisory Team recommends that the role of the CMU within the City Administration also be clarified. The Advisory Team recommends that shareholder support services be assigned elsewhere, in order to focus CMU on the client role. In addition, it is recommended that the role of supporting Council to develop tariff policy be assigned to the Finance Department. CMU will be responsible for taking this policy and formulating tariff methodologies for approval by Council,

and for negotiating tariffs with UAC's. This separation of policy and implementation is of critical importance.

Based on these recommendation, the Advisory Team developed a suggested organizational structure for the CMU, as shown below. If the CMU is to be assigned additional duties, such as the “office of the shareholder”, then that office should be clearly separated in the CMU organisation, so that different individuals perform the client and the shareholder role.

Suggested Organizational Structure of CMU



1.7 Recommended Actions and The Way Forward

The Advisory Team sees the following as next steps in developing an implementation strategy for the CMU:

- Clarify the roles of Client and Shareholder
 - Political organisation – assign shareholder responsibility
 - City Administration - assign “office of the shareholder” to an appropriate location
- Present revised CMU Business Plan to Council, adapting to redefined role
- Develop CMU's Capacity
 - Organisational structure & function
 - Staffing & compensation
 - Training & development
 - Adopt procedures & methodologies

2. INTRODUCTION

2.1 Basis for PADCO's Role in Developing the Implementation Strategy

The Johannesburg City Council has designed and implemented a wide range of reforms designed to improve the financial performance, efficiency and accountability of public service delivery. A key component of this reform was the transformation of twelve former municipal service departments and agencies into utilities, agencies and companies (UACs) under the Companies Act. A Contract Management Unit (CMU) was created to negotiate service delivery agreements under which the UACs provide either public services to the residents of the city or support services to the city administration. CMU is also charged with monitoring the performance of the service providers and compliance with the contracts. The Council requested specialist advisory inputs to ensure that international best practices were being employed by its Contract Management Unit (CMU).

PADCO was selected by the United States Agency for International Development (USAID) to provide Technical Assistance to the Contract Management Unit for that specific purpose. In addition, The World Bank, with funding from the Cities Alliance, also contributed funding and expert assistance to the Advisory Team.

2.2 Principal Players during the Analysis Phase

During the Analysis Phase, which spanned nearly three weeks in October 2001, the PADCO Advisory Team met with a variety of stakeholders. These included the entire staff of the CMU, three of the four Portfolio Committee Chairpersons of the City Council, and the Managing Directors or senior staff of all of the UAC's. In addition, informational meetings were conducted with consulting advisors under contract to the CMU; representatives of the National Department of Finance, and the Executive Director of Finance for the City.

2.3 Initially Stated Purpose of the Advisory Services

Prior to the Analysis Phase, when the needs of the Council were being initially defined, relative to the CMU, the Scope of Work focused on a review of the CMU Business Plan. The result of this effort would have been the preparation of an Implementation Strategy of Institutional Framework Recommendations that would strengthen the CMU in the execution of its stated mission.

The Analysis Phase made it clear to the Advisory Team members, that the issues were larger than merely the form, function, and staffing of the CMU. More basic questions were being raised as to the role, responsibility and authority of the CMU, and the channels of reporting for the UAC's

2.4 Redefined Focus of Advisory Services

In light of the observations that were made, and the inputs that were received, by the Advisory Team, it was determined that the focus of the Advisory Services should be redefined. In this regard, the Work Plan that was prepared early in the Analysis Phase stated that the Advisory Team would not be bound by the Business Plan of the CMU, as previously developed. Rather, the Advisory Team would identify the key roles to be played in contracting and supervising the

UACs, and recommend how these roles might be allocated among the Council, City Management and the CMU in light of existing law as well as international best practice. The intent of this broader approach was to provide an objective set of recommendations, as they relate to ensuring and protecting the public interest in the delivery of public services.

3. BACKGROUND OF IGOLI VISION AND CURRENT DIRECTION OF CITY COUNCIL

3.1 Creation of iGoli 2002 Vision

As the transitions in local government have been evolving throughout South Africa, and as the demarcation of municipalities has increased the overall size of the traditional municipal boundaries, Johannesburg was faced with ever increasing complexities of equitable public services delivery. The need to bring greater efficiency to overall operations, while still expanding services to more citizens, all in an environment of low or reduced operating and capital expenditures, dictated that something had to change. There was also a perceived need to reduce interference in day-to-day management so as to promote greater managerial autonomy and accountability.

It was in light of this challenging situation that iGoli 2002, a municipal government reform plan for Johannesburg was proposed and adopted. Essentially, iGoli 2002 was focused on transforming nearly all of the City's service activities into commercial entities of one form or another. It was hoped that such a transformation would allow the services to then have a wider access to much needed capital, improve accountability, de-politicise the management and delivery of services, while also strengthening management.

Although the legal process is not yet complete, the various service entities began to function as commercial companies under the South African commercial companies law in mid-2001.

3.2 Current Working Structure of Council and Its Perception of Duties and Responsibilities

When the Council, which is made up of 217 Councillors, is not in session, certain of its functions are delegated to an Executive Mayor, who is supported by a Mayoral Committee and defined Portfolio Subcommittees that deal with different areas of public services delivery or core Council activity. It is at the Portfolio Committee level that the new relationship with City Management is being defined.

The Councillors interviewed during the Analysis Phase said they understood the iGoli 2002 plan and model, but clearly want the Council to have more "hands-on" involvement in its day-to-day implementation, rather than leave it to the City Manager's Office. However, it appeared to the Advisory Team that this level of involvement was reversing some of the objectives of iGoli 2002, particularly as it addressed a de-politicisation strategy and the arms-length relationship with the UAC's.

4. CURRENT AND PROPOSED LEGISLATION IMPACTING RESPONSIBILITY, AUTHORITY AND OPTIONS OF LOCAL GOVERNMENT

From the local government perspective, South Africa has made, and continues to make, significant changes in the legislation affecting local government, and its responsibility and

authority to meet the needs of citizens in terms of governance and public services. In this regard, the key pieces of legislation are the Municipal Structures Act, the Municipal Systems Act, and the yet to be enacted Municipal Finance Management Bill.

4.1 Municipal Structures Act

This Act has been considered in the analysis phase and in the preparation of this Report from the perspective of attempting to understand the roles, responsibilities and authorities of the Executive Mayor, the Mayoral Committee, and the “Committees to assist the executive mayor”, which are known as Portfolio Committees in Johannesburg.

4.1.1 Executive Mayor

The position of the Executive Mayor is defined in sections 54 through 59. Of relevance to this Report is section 56, which addresses the “Functions and Powers of Executive Mayors”. It appears to the Advisory Team that most of these functions and powers fall into the realm of policy development and oversight rather than the direct implementation of policy and management of the services and activities of the City. Nevertheless the Executive Mayor’s responsibility to “oversee the provision of services ...in a sustainable manner” (Section 56 (3), e) could be interpreted to leave open the door for more direct involvement.

4.1.2 Portfolio Committees

Section 80 of the Act allows for the establishment of Committees to assist the executive mayor. It is under this section that the Portfolio Committees have been formed, and hence their frequent reference as Section 80 Committees. The significance to that reference, as explained by City staff, is that Section 80 committees can take decisions. Therefore they must have a committee membership that is politically representative of the political composition of the municipal council.

The executive mayor may delegate powers and duties to these committees. In Johannesburg, many of the Executive Mayor’s powers with regard to the provision of services have been delegated to various Portfolio Committees.

4.2 Municipal Systems Act, 2000

A balanced understanding of this Act and of the proposed Municipal Finance Bill is critical in attempting to consolidate the recent corporatisation of municipal services by the City of Johannesburg and create an appropriate supervisory framework.

As mentioned earlier, among the key issues that need to be addressed is the clarification of the respective roles and responsibilities of the various parties, in particular:

- the Council (as both the responsible authority and policy maker for the services on one hand, and as shareholder of the UACs on the other),
- the Office of the City Manager (as the signatory of the SDAs on behalf of the Council),
- the CMU (as the agent of the Office of City Manager charged with monitoring the performance of the UACs,
- the UAC’s (as service providers) and
- the Boards of Directors of the UACs (as agents of the shareholders).

Chapters 6, 7 and 8 of the Municipal Systems Act address several relevant themes such as tariffs, the provision of services by external mechanisms, performance monitoring and the delegation and separation of functions.

4.2.1 Service Tariffs

Section 74 of the Act deals with tariff policy. It requires municipal councils to adopt and implement tariff policies based on the principles of full and equitable cost recovery, charging in proportion to actual use, transparent subsidies, access of poor households to basic services, and the efficient and effective use of resources. It gives priority to considerations of economic, financial and technical sustainability of services with very limited scope for other considerations. It effectively rules out setting tariffs on the basis of political expediency.

The Johannesburg Council must develop tariff policy that is based on objective technical and economic criteria for arriving at a rational tariff. Although the role of the CMU is discussed later in this Report, it can be said here that with technical, economic, and objective tariff policy, the responsibility for negotiating tariffs on behalf of Council should be left to the professional staff. Council has the right to approve the final negotiated tariff.

4.2.2 Provision of Services

Section 76(b)(l) provides for the provision of services by an external mechanism by entering into a service delivery agreement (SDA) with a municipal entity. This is the part of the Act that authorizes the direction taken by City of Johannesburg Council.

Section 81 addresses, “Responsibilities of municipalities when providing services through service delivery agreements with external mechanisms”. This is particularly relevant to the management strategy that is being implemented in Johannesburg.

Subsection 81(1) serves to emphasize that delegation through a service delivery agreement does not diminish the municipality’s responsibility to provide services. This point is nevertheless consistent with the principle of according sufficient managerial autonomy to either municipal or private sector entities.

It is important to note that subsection 81(1)(d) is very clear when it states that a municipality must, “within the tariff policy determined by the municipal council in terms of section 74, control the setting and adjustment of tariffs by the service provider for the municipal service in question”. It is the opinion of the Advisory Team that this can be interpreted to mean that the municipal council must ensure that rules governing the setting and adjustment of tariffs are consistent with the principles set out in section 74, and that these rules are respected. In that regard it seems to protect against arbitrary changes tariffs. This point is further reinforced and clarified in subsection 81(3) which allows the service provider to adjust tariffs periodically in a manner that is consistent with the service delivery agreement. Thus interpreted, subsection 81(1)(d) supports sound corporatisation practice.

Subsection 81(2)(b) allows the municipality to “pass on to the service provider ... funds for the subsidization of services to the poor.” This is a progressive concept that is consistent with the tariff principles established in section 74 and with sound corporatisation practice. If implemented, such direct subsidy payments would make it possible to eliminate the economic and financial distortions caused by cross-subsidies.

4.2.3 Performance Management

Chapter 6, Performance Management, deals with the need to monitor the adequacy of services from the client's point of view. It provides a foundation for what could be considered as the function of the Contract Management Unit. The Chapter is structured very clearly to address:

- Establishment of performance management system
- Development of performance management system
- Monitoring and review of performance management system
- Reporting requirements

Under subsection 39(a) of the Act, the executive committee or the executive mayor is responsible for the development of the performance management system. However, subsection 39(b) states that the executive mayor must “assign responsibilities in this regard to the municipal manager”.

Sections 40 and 41 establish the basis for defining the functions of a Contract Management Unit. Specifically, section 41 lists what a municipality must do to establish a performance management system. Read in the context of a service delivery agreement scenario, these sections provide the framework that a Contract Management Unit, in its capacity as the representative of the client, would use to monitor the compliance of service providers with the SDA-specified indicators of the adequacy and efficiency of services. The monitoring arrangements must be such that the requirement of subsection 41(2) would be satisfied. That is, “the system must be devised in such a way that it may serve as an early warning indicator of under-performance.” In the opinion of the Advisory Team, this requirement does not imply the need for day-to-day contact with, or oversight of, the service providers. On the contrary, by establishing a system of measurable indicators and targets and regular reporting and analysis of performance, sections 38 through 41 are clearly meant to provide for an arms length monitoring arrangement that does not interfere in day-to-day management.

Experience elsewhere has shown that the best way to hold service providers accountable and encourage good performance is to give managers adequate autonomy to control outcomes. The principle of managerial autonomy and accountability is one of the key principles underlying the move to corporatise public services.

4.2.4 Delegation

Chapter 7, Part 3, Delegation System, is also important to this analysis. Subsection 59(1) specifies that “a municipal council *must* develop a system of delegation that will maximize administrative and operational efficiency...” (*italics added*). However, subsection 59(1)(a) specifically prohibits the council from delegating certain powers such as the power “to set tariffs” and “to decide to enter into a service delivery agreement”.

Taking the second first, it is reasonable for the Municipal Council to reserve the right to decide to enter a municipal service agreement, both from a policy standpoint, and later, in authorizing the signing of an agreement. The issue of “the power to set tariffs” must be interpreted in the context of other sections of the Act that were cited earlier (sections 74, 81(1) and 81(3)). That is, the council must adopt tariff policies and rules, and take steps to ensure that these policies and rules are enforced. Delegating responsibility for implementing (applying) tariff policies and rules would not contravene section 59(1).

4.2.5 Separation of Functions

Section 38(c) of the Municipal Systems Act, 2000, requires the municipality to “administer its affairs in an economical, effective, efficient and accountable manner”. Numerous provisions of the Act encourage the separation of policy functions from administrative and operational functions. For example, section 51(k) specifically requires the delegation of responsibilities to the “most effective level”. Section 53 requires the clear specification of roles and responsibilities. Section 55 specifies that municipal administrations must perform their duties subject to the policy directions of the municipal council, and section 59 requires the council to retain power over key policy decisions.

4.3 Municipal Finance Management Bill 2001

At the time of the preparation of the analysis and implementation strategy contained in this Report, the Municipal Finance Management Bill was still under review and modification as a draft bill. However, the draft had evolved enough to provide some clear insight as to how it proposed to address the responsibilities of a municipality as shareholder of corporate entities, and the financial management of such corporate entities created by municipalities. The version of the Bill that was reviewed was the one printed in the Government Gazette, 31 August 2001. Chapter 9 of the Bill addresses Municipal Entities.

4.3.1 Appointment of Boards of Directors

Under section 53, the bill makes it clear that it is the intent to “de-politicise” the appointment of members of the boards of directors, by requiring the Municipal Council to obtain and consider the recommendations of the municipal manager.

Further to that, section 52 goes to great length to minimize, if not discourage, the appointment of members of the Municipal Council to boards of directors or other governing bodies of municipal entities.

4.3.2 Reporting of Entities to Municipal Manager

Sections 57 through 59 detail the accounting authority and reporting requirements of the municipal entity. These three sections establish clear accounting/financial reporting relationships.

Although this bill may still experience revisions before finally being enacted into law, in its current form, it indicates that the financial management of the municipal entity is the responsibility of the chief executive officer of the municipal entity who reports to its board of directors. Secondly, section 57 (5) requires the chief financial officer of the municipal entity to report to the municipal manager, who in this case is not only the chief accounting officer of the municipality, but presumably also the representative of the shareholder: “To the extent that the accounting authority of a municipal entity is accountable to the municipality exercising sole or joint ownership control over the entity, the accounting authority must discharge that responsibility through the municipal manager...”

4.3.3 Preparation of Business Plan

Section 62 addresses the requirement for the adoption of an annual or multi-year business plan for the entity. The entity must submit its business plan to the municipality or municipalities

exercising ownership control over it, for approval. Clearly, this section is addressing the relationship between the entity and its owner (shareholder).

5. THE ROLE OF GOVERNMENT AND CORPORATISATION

5.1 The Objectives Of Corporatisation

The purpose of this chapter is to re-examine the objectives of corporatisation as well as the characteristics of the various UACs, so as to set the stage for clarifying the roles of the various actors, in particular the CMU.

While a well-developed cost accounting and revenue allocation system for government departments can help to reveal the true cost of services and improve financial management, corporatisation represents a more profound institutional reform that can potentially go much further by giving service providers more autonomy, creating incentives for efficiency and innovation, and making managers more accountable. But these benefits can be achieved only if the overall institutional framework is carefully designed to distinguish the roles of the various actors and avoid conflicts of interests.

5.1.1 Improved Financial Viability and Efficiency

One of the key objectives of corporatisation in Johannesburg was to reduce the financial burden associated with the services the city provides. A service is financially viable only if its revenues are adequate to cover costs. If the service provider is able to charge user fees that cover the full cost of service, and collect those revenues, then it is truly financially autonomous. If it receives a subsidy, it may be considered financially viable, but it would not be financially autonomous.

Efficiency is another matter. In a competitive market, prices are set by the most efficient producers, so corporatised municipal services that are able to compete with private services are both financially viable and efficient. However, services that are monopolistic (such as water supply and electricity) are not subject to competition *in the market*, so other methods of promoting efficiency must be developed. The challenge of economic regulation is to set tariffs of such services at levels that both promote efficiency and allow the service provider to cover all reasonable costs.

If a service provider (whether subject to competition or not) is not able to charge prices that cover all costs, but the municipality nevertheless wishes to continue to provide the service, then the City must provide for a subsidy or instruct the service provider to structure tariffs for different users so as to generate a cross subsidy adequate to cover the shortfall. One of the key advantages of corporatisation is that it helps to make subsidies more transparent so that municipal decision makers and the public can see how much the service is costing the tax payers (or a particular group of users in the case of cross-subsidies) and determine whether the expenditure or cross subsidy is justified. This is true only if the corporatised service pays the full cost for all inputs. If not, the subsidy tends to be hidden, for example, if the service provider pays less than full cost for power.

5.1.2 Greater Autonomy and Accountability

The corporatisation model that has been applied in Johannesburg was intended to give the service providers greater autonomy and freedom from short-term political influence. Boards of

Directors were chosen from both the public and private sectors with a view to ensuring objective corporate governance. Under this model, the Boards of Directors appoint the managing directors of the companies who in principle have autonomy to manage day-to-day operations, sign contract with third parties, allocate resources within approved budgets, hire and fire staff, etc., subject to the terms of their SDAs.

Autonomy makes it possible to impose greater accountability. A Board of Directors that controls business planning and appoints management can be held accountable for financial results and long-term viability of the company by shareholders (in this case the Council). A manager who controls key operational decisions can be held accountable for outputs and his/her contract may be terminated by the Board of Directors if the agreed results are not achieved.

5.1.3 Attracting Investment Finance

By promoting financial viability and ensuring managerial autonomy and accountability, corporatisation paves the way for attracting commercial lending (for expansions and improvements) that does not require the backing of the city. There are two benefits to this: First, the service providers will be able to qualify for investment finance in their own right, regardless of the financial health of the city as a whole. Secondly, the city will not have to assume the risk of commercial loans and will be able to allocate its own resources to other public needs that are not commercially viable, such as libraries, recreation and health.

5.1.4 Payment of Remittances or Dividends

Historically the electricity and water services and the fresh produce market have contributed general revenues to the municipality, over and above the estimated cost of providing these services. At the time of corporatisation, it was decided that these three UACs would continue to pay an annual remittance to the city. Although this remittance has been referred to as a “dividend”, it is not calculated on the basis of the value of the city’s equity in the company and is therefore not really a dividend, but rather a tax. The city finance department acknowledges that this form of taxation is not equitable, but the city currently depends on this revenue so it cannot be eliminated immediately. More equitable forms of taxation would be preferable, but unfortunately the restrictions on local government’s taxation powers are problematic. However, the payment of a true dividend to the city may be justified. If so, the dividend should be linked to the value of the city’s equity in each company, and provide a reasonable return on that equity. Another alternative that is being considered is the payment of a rent or debt service to the City based on the sale value of the UAC.

5.1.5 Defining a Strategy for each of the UAC’s

Now that the conclusion of the transition phase is in sight, some thought needs to be given to developing a long-term strategy for each of the UACs. The long-term strategies should take into account the basic economic characteristics and regulatory requirements of each service, projected changes in its market, and its potential for further transformation. Some services will always be pure public goods. Others have the potential to become commercially viable and perhaps attract private participation. Some may evolve over time from primarily public to private as a result of higher incomes and standards of living. (For example, domestic solid waste collection may become a private good over time.)

5.2 Economic Characteristics And Different Contractual And Regulatory Requirements Of The UAC's

The UACs are not a homogenous group as regards their economic characteristics and market conditions. As a result, some require primarily contract management while others require more policy input and regulation (to pursue social objectives and compensate for market failures). For others the City is not really a client, but only the shareholder. To take full advantage of the benefits of corporatisation and rationalize shareholder, client and regulatory functions, it is essential to recognize the differences. They can best be understood when the UACs are grouped with regard to the following parameters:

- Whether the services are delivered directly to the residents of the city or as support services to the city administration,
- Whether the services are monopolistic, natural or *de facto*, or are subject to competition,
- Whether the services provided to the residents are private goods for which users pay on the basis of consumption, or public goods which are paid for out of general revenues or for which users pay only nominal fees.

On the basis of these parameters, we have classified the UACs in five groups. Note that while these are similar to the original groupings, i.e., utilities, agencies, and companies, this classification uses slightly different criteria which allow us to distinguish among them on the basis of contract management from the point of view of the City as client, and their policy and regulatory requirements. Certain UACs that offer more than one type of service may fall into more than one group, because some components of these services may be commercially viable and/or subject to competition, while others are not. The components that are not commercially viable may be justified if they generate economic, educational, cultural, environmental benefits that individual users are not willing to pay for. However, they must be funded by direct or cross subsidies. The oversight of these services must therefore ensure that the subsidized services are truly beneficial and weigh their benefits against the costs to ensure that the allocation of subsidies is rational. Tariffs for the non-commercially viable services must be regulated to ensure that net benefits are maximized. The theatre, the zoo and JDA may be able to exploit their unique nature to generate surpluses from commercially viable activities. Such innovative ways of generating revenues should be encouraged but should not undermine the core services.

It is worth noting that these groupings may be subject to change or correction. The purpose of this exercise is not to group the services definitively, but rather to demonstrate the different supervisory demands imposed by different economic and market conditions.

5.2.1 Essential Services for Which Users Pay on the Basis of Consumption

The following are services under this category:

- Johannesburg Water
- City Power
- Igoli Gas
- Pikitup's domestic collection service
- Metrobus' routes that are not subject to competition because they are not commercially attractive

These are essential services (as defined in the Municipal Systems Act, 2000) and are monopolistic (whether natural or *de facto*) in the areas where they operate. Of all the UACs, these require the most supervision. The service conditions and quality must be specified and monitored through the SDA. In addition, because they are monopolies, tariffs must be regulated, consumer rights must be protected, and mechanisms to address consumer concerns and complaints must be established.

Although Johannesburg Water, City Power and Igoli Gas are natural monopolies such that competition *in the market* is not practical, they could in theory be subject to periodic competition *for the market*. Such competition might promote greater efficiency if it is managed effectively. Domestic waste collection services are not a true natural monopoly although it is usually more practical to have a single company operate in each zone of a city. Given the size of Johannesburg, several contracts for exclusive zones could be awarded to different companies, creating a more competitive environment that would reduce fees.

5.2.2 Public Services for Which Users Pay No or Nominal Fees

The following are services under this category:

- Pikitup street cleaning and disposal of domestic waste
- Johannesburg Roads Agency
- City Parks
- Johannesburg Zoo
- Johannesburg Trading Company

Most of these service providers have only one client, the City of Johannesburg. Residents of the city do not pay a fee (or pay only a nominal fee) each time they use the service. With the exception of the Zoo and the Trading Company, these do not require regulation of user fees and customer relations. However, they do require contract negotiation, management, and monitoring and enforcement of service quality.

Pikitup domestic disposal services are currently operated primarily like public goods. The waste fee that households are charged probably does not cover the cost of disposal. Under the current conditions, it is difficult to force households to pay the full cost of such services that have broad environmental and health benefits. (The waste fees that commercial and industrial users pay is supposed to cover the cost of disposal. The cost accounting system that is currently being implemented will make it possible to determine appropriate fees.)

Despite being public goods, the management and operation of some of these services could be subject to competition *for the market*. Moreover, if they are not subject to economies of scale, there is no economic reason why the service providers should be monopolies. The Johannesburg market is large and several contracts could be awarded to different service providers for street cleaning, road maintenance and parks management. If competition for contracts and contract enforcement were effective, considerable efficiencies could be realized and the burden of negotiating SDAs would be greatly reduced.

5.2.3 Administrative Support Services

The following are services under this category:

- Propcom
- Fleet
- Proposed IT contract

These UACs or private contractors provide administrative support services to the City administration as well as other UACs. They have no interaction with the general public. However, they do have clients within the administration, who pay on the basis of consumption of services. Thus a schedule of fees must be negotiated and client relations are a component of service quality. Like some of the public services in the previous category, the management and operation of these services could be subject to competition *for the market*, which, if effective, would help to control costs and reduce the burden of negotiating fees.

5.2.3 Private Services Subject to Competition

The following are services under this category:

- Fresh Produce Market
- Civic Theatre
- Pikitup commercial and industrial collection/disposal
- Metrobus' commercially viable routes

In theory, an SDA on behalf of the City as client is required for these UACs only if the Council in its role as policy maker wishes to mandate and subsidize certain non-commercially viable goods or services or require the service provider to cross subsidize certain users. If a service is commercially viable and requires no subsidy, the City's relationship to the UAC should be strictly that of shareholder and there is no need for an SDA *per se*, but only a shareholder compact.

5.2.4 Special Case

The following are services under this category:

- Johannesburg Development Agency

JDA is a special case because it is not so much an administrative support service as a strategic activity and it does interact with other actors and clients outside the city administration. The service it provides is more like a core function than that of some of the other services, so it might be difficult to subject it to competition *for the market*. Even though it is expected to be commercially viable, its special mandate to promote economic development warrants an SDA.

6. Clarifying the Role of Shareholder and Client

6.1 City Council as Shareholder

The City of Johannesburg, not unlike nearly all major municipalities, has created a large amount of physical assets to serve the needs of the City and its people. In the case of the City of Johannesburg, it has chosen to take the functional groupings of these assets (normally "departments"), and transform them into commercial companies under company law in South Africa (corporatisation). In so doing, the City has gone from being the owner of assets, to the

owner of shares in companies, which in turn, owns the assets and represents them on their respective financial balance sheets.

As the 100% owner of the shares in each of the respective companies, the City has also chosen to name non-political Boards of Directors for each of these companies. It has charged these Boards of Directors to set policy and oversee the management of these respective companies. These Boards of Directors require the respective managing directors, and their management team, to prepare and submit Business Plans to the Board of Directors, that support the accomplishment of the service conditions of the SDA's and any other business objective that the Board approves for the company.

As shareholder:

“the Council retains responsibility and receives dividends in the case of utilities or provides subsidies in the case of agencies and certain corporatised entities. The Council also “regulates” the service in respect of the following: financial issues (such as tariffs and capital expenditures), human resources issues (such as skills development), delivery targets (maintenance of assets and addressing backlogs), and standards of customer care.”

What the City, as shareholder, has not done clearly is to indicate its desires for the ultimate development of each of these companies (the “end game”); the City's long term interest as an “investor” or provider of “working and investment capital” (subsidies); and the City's vision of the final commercial status of these companies.

6.2 City Government as Client

In accordance with legislation, the City of Johannesburg delivers services to its citizens by entering into a non-competed, Service Delivery Agreements (SDA's) with these newly created companies. From this perspective, the City Council, centred on the Executive Mayor, and acting through its Government (City Manager), is a “Client” of the respective companies for the delivery of the services defined in each of these SDA's.

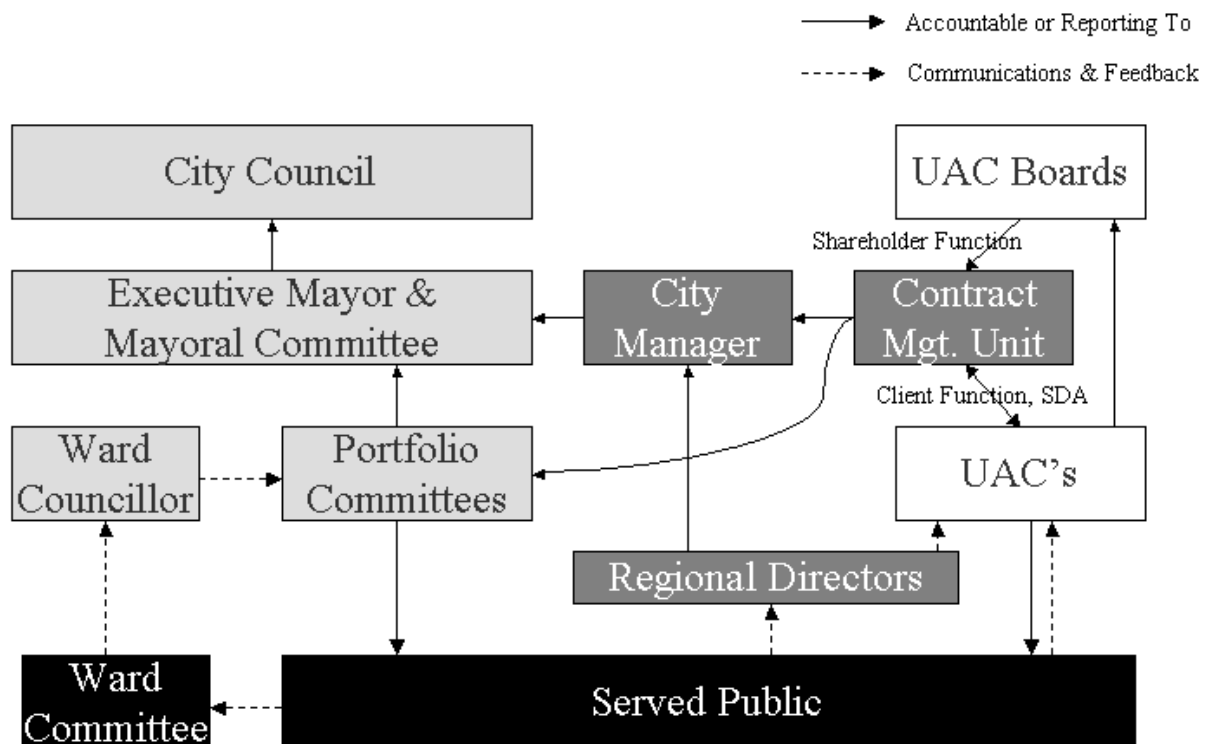
This “new” client role can be a very conflicting situation, when first implemented. It is only human nature to resort to prior behaviour, when reacting to service delivery problems in a City, and that is to start “directing” those individuals responsible for services delivery to do a particular thing or take a particular action. The problem is that under the new service delivery model, that the City Council has elected to implement, it no longer is authorized to “direct” the service provider. The vehicle for service is the SDA, and the option to the City Council is to require compliance with the SDA.

6.3 Why Differentiate Between Shareholder and Client?

There is much discussion within City Council and City Government, in Johannesburg, concerning the rights and duties of the shareholder, and the fact that the newly created companies are not necessarily providing services as agreed. The question is often: Who should do what about the situation? The heart of the matter is having a clear and consistent understanding about what is a shareholder and what is a client, and the respective roles and responsibilities of each.

To aid in this understanding, the Advisory Team has prepared a chart titled, Johannesburg Today. This is intended to depict the existing conditions as regards the organizational relationship structure with regard to the functions of the UAC's. This chart has been included within this section.

Johannesburg Today



6.4 Role of City Council Structure in Setting Policy and Citizen Advocacy

The City Council, in nearly all municipal structures, is the institutional body of the people, within a political jurisdiction. It advocates the interests of the people, arrives at collective solutions to problems that affect the people, and sets the policies necessary to guide the implementation of those solutions. In Johannesburg, this institutional body is a group of 217 elected City Councillors.

6.4.1 Executive Mayor and the Mayoral Committee

The Municipal Structures Act allows for the appointment of an Executive Mayor with defined delegated authorities and responsibilities from the City Council. The City of Johannesburg has

been established as such a municipality . This position of Executive Mayor is filled by an individual, appointed by the City Council, from within the Council membership. This structure, as defined in the Act, gives the Mayor executive powers to “run the City”. It is not clear, from the Act or the stated delegated authorities and responsibilities from the City Council, whether “run the City” means to be redundant to the City Manager, or that is more precisely, to carry out the policy formation and oversight role of City Council, in an executive and “hands-on” way, but that certainly seems to be the tendency.

Within the function of the Executive Mayor, a Mayoral Committee has been formed. The Mayoral Committee is made up of ten (10) City Councillors. Each of the Councillors of the Mayoral Committee chairs one of the Portfolio Committees, which are charged with the policy and oversight issues of the Council relative to some specific services or responsibilities of the City.

6.4.2 Portfolio Committees

Differing from the Mayoral Committee, the Portfolio Committees are not strictly decision making bodies, as they advise and monitor. They may however, decide to appoint consultants. They are known as Section 80 Committees under the Municipal Structures Act, and are composed along multi-party lines.

In the case of four of these Portfolio Committees (Municipal Services Entities; Municipal Enterprises; Community Development, Roads, and Parks; and Finance, Strategy and Economic Development), they are also the point of contact, on behalf of the City, in the Client/Service Provider relationship with each of the UAC’s. Their role is to translate the policies and service delivery objectives of the City Council, coming down through the Executive Mayor, to the City Government, who is then charged with implementing these directions. In turn, those four Portfolio Committees must present the implementation options and impacts, as determined by the City Government staff, back to the City Council for decision or approval. Under the current structure, the Portfolio Committees rely on the professional and technical capacity of the Contract Management Unit, in the Office of the City Manager, to implement the wishes of the City Council, as they relate to the UAC’s.

6.4.3 Ward Councillor/Ward Committees

It is important to note that the political structure in Johannesburg is designed to be as close to the people as realistically possible. To achieve this, Ward Committees are being formed within each political ward of the City. These Ward Committees are intended to be non-partisan bodies, and are chaired by the Ward Councillor. This structure provides one, of several sources, for the public to air and address its concerns in the areas of public service delivery.

6.4.4 Approving Boards of Directors for UAC’s

The City Council, in fulfilling the role of Shareholder with a “100% ownership position”, has the full right and authority to approve membership to the Boards of Directors of the various UAC’s. It must be remembered, from the review of the Municipal Finance Management Bill, under Section 4.3 of this Report, that the City Council “must distance” itself from actually naming the various Boards, by considering candidates provided to it by the City Manager. The City Council, in exercising its policy authority, can set minimum criteria for candidates to be nominated, but should not directly select the candidates for Board membership.

6.4.5 A Clear Role for City Council as Shareholder

This Section of the Report has tried to clearly frame and explain the two separate roles of City Council relative to the UAC's; the first as 100% Shareholder, and the second as client to the UAC's by way of a negotiated SDA, that is fully administered by the Contract Management Unit in the Office of the City Manager.

As a client, the City Council will focus on formulating policy guidelines for service levels, access, and tariffs.

As a shareholder, Council will give strategic direction to UACs. Council will appoint the members of the Board of Directors, and auditors. The City Council (Executive Mayor/Portfolio Committees) should not "cross the line" and involve itself in the management of the UAC's in any way, except to the degree that it approves the nomination of members of the Boards of Directors.

The City Council should clarify how the shareholder function is managed and administered within the City. As a minimum, this function includes holding the "shares" in each of the companies, soliciting and evaluating candidates for Board of Director positions, and receiving the "dividend payments" that are negotiated in selected SDA's. This is currently considered a responsibility of the Contract Management Unit, but such an arrangement creates a conflict of interest. The Contract Management Unit must negotiate, at arms-length, with each of the UAC's, therefore it cannot be in a position of nominating the Boards of Directors of these UAC's.

The recommendation is that the shareholder function be placed in an appropriate location. There are several options. One option may be the Office of the City Manager, another is the office of the Executive Mayor, and another is the Finance Unit in the Office of the City Manager. If it is to be retained within CMU, it must be clearly differentiated, with different staff carrying out the shareholder and the client roles.

6.5 Role of City Management Structure in Execution of Policy

The iGoli 2002 vision was, "that the City would work through a combination of new political governance structures, a core administration, regional administrations, and utilities, agencies and corporatised entities." The Executive Mayor and the Portfolio Committees relate to the administration of the City by way of the chief executive officer (City Manager). It would appear that the intent was to have a clear separation of authority and responsibility (power) between the policy role and the execution role.

6.5.1 City Manager

The City Manager is the Chief Executive Officer of the City in the performance of the responsibilities and services of the City, as stated in Law or as determined by the City Council.

6.5.2 Executive Directors

The senior management, within the Office of the City Manager, is made up of four Executive Directors consisting of the areas of Finance, Corporate Services, Planning, and Contract Management. For purposes of this Report, it is the specific functions of Contract Management that are under consideration. However, as was seen when the issue of the role of the

“shareholder” was discussed in the Report, the other Executive Director functions have a role in the total iGoli 2002 model and operational structure.

6.5.3 Regional Directors

Just as the political structure, as described under 6.4.3 of this Report, reaches down to address the needs of the people through its Ward Councillor/Ward Committee structure, so does the Office of the City Manager. In this regard, the Metro City is divided into twelve Regions with a Regional Director assigned to each, who is physically located within the Region and is accountable to the City Manager.

These Regional Directors directly concern themselves with the management of the delivery services in the following areas: health, social, housing, library, and sport/recreation within their Region, while also coordinating with the UAC's, as appropriate, in terms of their various activities in their Region.

The Regional Directors are also an interface with the people in terms of hearing their concerns and addressing their complaints, when it comes to services that they should expect from the City.

6.5.4 A Clear Role for City Management as Client's Representative

If the City of Johannesburg is still committed to the vision and goals of iGoli 2002, as originally structured, it is strongly recommended that the line between policy formulation and policy execution be kept sharply defined. Specifically, as it relates to the delivery of public services and the performance of the UAC's, it is the Office of the City Manager that is structured and staffed to represent the needs of the Client (City Council) on a day-to-day basis.

Portfolio Committees need to be kept informed of the performance of the UAC's that are within their areas of responsibility, and need to be advised as to actions that are being taken, when non-compliance has been identified or reported in a particular area. This is the responsibility of the Office of the City Manager, through the competence and capacity of its Contact Management Unit.

7. Clarifying the Relationship of the UAC's with City Council and City Government

With the development of the concept of the UAC's under the iGoli 2002 model, Johannesburg has not taken a “business as usual” approach to governance and municipal management. However, like with any major change, there is the “good news” and the “bad news”. The good news is that there is change, the bad news is that “change requires change”. This can never be more true, than when one considers the situation that the UAC's face under this new structure, if traditional Council behaviours do not change or are re-applied.

This section of the Report has been written as the recommended way to look at the “relationship” issue as it concerns the functioning of the UAC's.

7.1 UAC Entity Accountable to Board of Directors

The UAC's are corporate entities and are established under South African company law. Consistent with company law, a Board of Directors has been appointed for each UAC company.

Like any company, the managing director and the senior management are directly accountable to the Board of Directors, who represent the interests of the shareholder.

Even though these UAC's are effectively owned by the City Council, as 100% shareholder, this should not change the company/board of directors relationship.

Therefore the recommendation is fairly direct: "Name good board members and hold them responsible for management."

7.2 Board of Directors Accountable to City Council

Having defined the relationship of a UAC entity to its Board of Directors, above, this condition is still not a license to ignore the City Council. City Council is still the 100% shareholder and names the Board of Directors. Since all boards of directors, in a corporate world, are accountable to their shareholders, then there is no question that the Board of Directors of a UAC entity is accountable to the City Council. However, the accountability is one that addresses the interests of the Council as owner, not as client.

7.3 UAC Entity Reporting to City Government

Since it has been established, by recommendation above, that the City Government (City Manager) is the proper representative of the Client (City Council), then any given UAC entity must report its performance to the City Manager, as defined in a SDA. Similar to the position of the City Council as shareholder, which does not interfere with the management of the business of the UAC entity, likewise, the City Manager, in a reporting line with the UAC entity, is not engaging the UAC at a business level, but at a service delivery level (SDA).

7.4 Identification/Negotiation of Key Performance Indicators (KPI's)

The City Manager, utilising the capabilities of its Contract Management Unit (CMU), provides the technical/legal/ financial support to the Portfolio Committee to identify key performance indicators (KPI) that the Portfolio Committee wants to negotiate into the SDA for that UAC entity. This can be an "advisory" service, initially, as the CMU assists the Portfolio Committee in identifying the cost/benefit impacts of each KPI.

Once the Portfolio Committee has settled on those KPI that it wishes to capture in a SDA, it then directs authorizes the CMU to proceed to communicate them to the respective UAC and to schedule negotiation sessions to arrive at a mutually acceptable SDA.

7.5 Preparation of Business Plan

The idea of the preparation of a five-year business plan is part of the normal practice of companies in a normal business environment. Consequently, it should be equally required of UAC's. The problem that needs to be considered, and therefore the question that needs to be raised is: "Who is asking for the business plan and why?"

Currently, the practice is that the business plan is submitted to the CMU for review and approval, before it is made an appendix to the SDA, which will then go to the Portfolio Committee for approval, before going to the City Council. This creates a very confusing set of actions and involvements.

In the traditional business-school sense, a classical business plan is management's proposal to the Board of Directors on the conduct of the business. The business plan defines the factors affecting the business, both positively and negatively; presents the growth opportunities of the business and the actions that are proposed to capitalize on those opportunities; states the capital needs of the business to implement those actions; and projects the revenues and expenses of the business based on the proposed business actions.

We note that the Johannesburg City Council has defined business plan a bit differently – as an annex to SDA. To the extent that the Municipal Finance Bill (if enacted) requires it to be defined, it may then take a shareholder-like quality.

The contents of a classical Business Plan does not need to be known, or should be known, by the clients of the business. Normally, the CMU or the Portfolio Committee should not be involved with this business plan. Normally, we'd expect the CMU to have a right to ask for a copy of an independent auditor's report on the business, to assess its financial strength.

The business plan, if needing to be reviewed, beyond the Board of Directors, needs to be reviewed by the Shareholder. Perhaps it needs to be adopted at the annual general shareholder meeting. If there is to be any review of it, then it would be done by the administrative unit of the City assigned the Shareholder function. Again, the shareholder/client distinction is important. The delineation needs to be made clear, so that the behavior of the players is consistent with sound corporate practice.

7.6 Negotiation of Service Delivery Agreement (SDA)

The place where a UAC entity (Company), the Government (Contract Management Unit), and the City Council (Portfolio Committee) should come together, and be seriously involved, is the negotiation of the Service Delivery Agreement. Ultimately, this is what iGoli 2002 is all about. It is about securing quality, reliable, cost-effective services for the residents of Johannesburg in a business-like manner with an arms-length, commercial agreement. It is in the SDA where policy compromises with economic reality to create service delivery standards and price.

It is not about whether the UAC entity should paint its trucks green or yellow, or whether it should buy a particular backhoe, or whether it should relocate its headquarters offices. Rather, It is about service, quality and price. If these cannot be met, to the satisfaction of the Portfolio Committee, and therefore City Council, then City Council can change policy or authorize the Contract Management Unit, through the Portfolio Committee, to identify alternative service providers. With this authorization, the CMU can initiate a tender process, and the competitive market can be the final determinate of price, for a defined service and quality level.

8. Clarifying the Role and Responsibility of the Contract Management Unit

In this Section of the Report, the Advisory Team will draw upon all of the preceding information, which has been developed and presented to provide a foundation for addressing the CMU, within the legal and administrative structures that actually exist in South Africa, and within the City of Johannesburg. This is important to the Advisory Team, since it makes little sense to superimpose a model that has no underlying authority in existing law or governance.

The CMU has prepared an Organizational Structure, which was presented to Council and approved on 13 September 2001. With that approval, it was understood that the CMU would

come back to Council, within one year, to reaffirm or make amendments to that original Organizational Structure.

The Advisory Team has reviewed that Organizational Structure, as a point of information, but has not focused on trying to optimise it. Like the existing Business Plan for the CMU, the Advisory Team has attempted to take an unconstrained look at the situation facing the City of Johannesburg, in implementing its UAC strategy, under the iGoli 2002 model, and to address all of the factors affecting success in implementing this model.

8.1 CMU as Integral Part of City Government and Corporatised Public Sector Management Strategies

It can be said, without equivocation, the CMU is an integral part of City Government and functionally reports directly to the Office of the City Manager. It exists there because the City of Johannesburg, within the principals of the iGoli 2002 model, chose a direction of increased corporatisation to improve performance and delivery of public services. Therefore, the CMU is a unique management tool that has been created by Council, within the Office of the City Manager, to ensure that the Council fulfils its obligations under Section 81 of the Municipal Systems Act.

8.2 Differentiating between Regulation and Contract/Compliance Management

There has been considerable discussion, in the past, as to whether the CMU was a regulator. This thinking comes, somewhat, from the fact that the Municipal Systems Act refers to the “regulatory” duties of the Municipal Council in the provision of services. The logic then flowed that since the CMU, as a part of the Office of the City Manager, was the implementing arm of Council relative to the public services of the UAC’s, then therefore, it would fulfil this “regulator role” within the definition of its delegated powers.

The fact is that the delegated powers of the Executive Director of the CMU, as delegated by Council, speak to such actions as: “conduct/execute transactions, management of contracts, and provision of recommendations, all in support of Council decisions or interests.”

Therefore, what the CMU actually does is “regulate” the UAC’s by contract. It does this by monitoring the compliance of the UAC’s on the basis of the conditions of the contract (SDA). However, it is not an “independent” regulator in the strict sense of the word.

8.3 Differentiating between Compliance Management and Business Monitoring

Having drawn this distinction, above, between regulation and contract management/ compliance management, it is now equally important to draw a distinction between compliance management and business monitoring, from the perspective of the CMU.

The Municipal Finance Management Bill, although not an Act, has been available in draft form for some time, and has guided the evolution of the relationship of the UAC’s, the CMU, and the Council. In that Bill, as pointed out previously in this Report, there is a requirement for Municipal Entities to prepare a Business Plan. Since it has been assumed, by Council and Officials, that the CMU represented the shareholder, then the logical place for the Business Plan to be reviewed and approved was in the CMU. In fact, this went a step further in this regard, and the CMU often involved itself in the preparation of the Business Plan, working along side the UAC’s.

This Report has clearly stated why the CMU cannot assume this role and therefore, there is no need to repeat it here. It is sufficient to say, regarding this issue, that the Business Plan must be reviewed by the Finance Unit of the Office of the City Manager, acting in its role as fiduciary trustee of the shareholders interests.

Given this logic, then we would not have expected the CMU to be interested in the business plan of the UAC (company). Certainly, the CMU should be interested in the terms, conditions and performance measures negotiated into the SDA. This is what they monitor (regulate) in their contract management role. However, these very measures are what is contained in the first generation Johannesburg business plans, along with projections of performance. These projections cover both client-oriented KPIs (service level and quality) as well as shareholder-oriented KPIs (financial and strategic). It could have been disaggregated, but Council elected to use one document for both purposes.

It is not contradictory logic, however, for the CMU (acting on behalf of client) to request a copy of the independent auditor's report on the financial condition of the Company, to assess the financial strength of its service provider, or to assess the profitability of their operations and the types of financial reserves that they have built. It is also not contradictory to request detailed information on the capital programs that the Company plans to undertake to achieve a negotiated service standard or service reliability. Likewise, it is not contradictory to request detailed information on the Companies' tariff collection rate history. These types of requests, and others, allow the CMU to assess the soundness of the programs proposed and the fairness of the basis for arriving at a proposed tariff.

What the CMU must not do, is to engage in analysing how the Company performs its business and directing the Company to make changes in those business practices. At that point, it will cross a line that then prevents it from being critical of the Company's performance.

8.4 Functional Interactions of the CMU with Council and Government

In the final analysis, it has to be clearly stated, or restated, that the CMU is an arm of City Government, as a part of the Office of the City Manager. However, City Government exists to implement the policy of City Council, and to ensure that the City is in compliance with all Acts that define the powers, duties and responsibilities of municipalities. In this structure, there is a unique balance for all municipal officials, as they work with the Council, Executive Mayor and Portfolio Committees, as a resource to, and implementers of, policy, and also as part of a management team, under the City Manager.

When it comes to the CMU, this works best when the Council/Executive Mayor/Portfolio Committee, understand their role in the iGoli 2002 model, and do not "over-reach" in attempting to "run the business" of providing municipal services.

In this way, the CMU can assist in policy making, by serving in the role of advisor to the Portfolio Committee to inform the Committee on the potential cost impacts of policy options, or on industry experience regarding the chances for success for a defined policy. Once policy has been decided, then the CMU takes on its implementation role and moves to capture the new policy in the SDA with the service provider.

8.5 Assessing Proper Roles and Capacities within City Government

It was apparent to the Advisory Team that the CMU either undertakes, or is asked to undertake, roles and duties that either do not belong in the CMU, given what we perceive as the CMU's primary role (acting on behalf of the City as client). In fact, we regard some of these activities as a conflict of interest, if performed by the CMU.

The first of these has been mentioned previously and is repeated here because it is extremely important, and that has to do with the Shareholder duties and responsibilities. This cannot be in the CMU, as currently constituted, and it is recommended that this is placed in an appropriate location as the "Office of the Shareholder". Correspondingly, the Business Plans of the various UAC's should be submitted to the Office of the Shareholder since the Business Plan, is approved by the Board of Directors of a UAC and then presented to the Shareholder, as contemplated by the Municipal Finance Management Bill.

Another issue, which is internal to the Government, is the use of the Legal Services Section of the Corporate Services Unit. At this time, the CMU undertakes all of its own legal needs by contracting with private firms. The need to contract with outside firms may be appropriate, but it should be a shared decision with the Legal Department, and the Legal Department should take ownership for the quality of services in this regard.

8.6 Description of Recommended Duties and Responsibilities of the CMU

Based on the issues addressed previously in this Report, the Advisory Team recommends that the Contract Management Unit be empowered, by the City Council, to have the following duties and responsibilities.

- Provide a research service to the various Portfolio Committees responsible for the delivery of public services, in the sectors served by the UAC's, in support of the drafting of policy by the Executive Mayor and the Mayoral Committee.
- Provide a procurement service for the delivery of public services, in the sectors served by the UAC's, to include the development of the scope of services, standards of performance, key performance indicators, and methods for monitoring performance. Work with the Legal Services Sector of the Corporate Services Unit to prepare standard contract language.
- Negotiate all SDA's with UAC's for the delivery of services, including the negotiation of tariffs and subsidies, in accord with policies set by Council.
- Review all reports required of UAC's in their respective SDA's, and report to the Portfolio Committee/Executive Mayor on the performance of UAC's, with recommendations for actions, as needed, to be approved or taken by the Council.
- Review and recommend action on the payment of all invoices submitted by UAC's.
- Resolve disputes on issues arising with UAC's relative to requirements stated in the SDA's, and work with the Legal Services Sector of the Corporate Services Unit to take legal action, as required, to protect the interest of the Council.

- Conduct independent customer satisfaction surveys to assess the performance of the UAC's and the effectiveness of the SDA's, in meeting the public policy objectives of Council.
- Based on input from Regional Directors or Ward Committees, provide for complaint/conflict resolution between the UAC's and the public.

8.7 Assessment of Current Capacity of the CMU to Successfully Perform Its Duties and Responsibilities

The CMU has some very talented individuals, however, the Advisory Team observed that they are often engaged in activities that do not relate directly to the duties and responsibilities outlined above for the CMU, namely Shareholder functions.

The two core functional areas of the CMU, based on the duties and responsibilities described above, can be summarized as follows:

- Research and Analysis
- Procurement and Contract Management

Within Procurement and Contract Management, the following major functions would be performed:

- Preparation of effective service delivery agreements, including specification of performance indicators and targets, rules governing tariffs, subsidies or cross subsidies (if any), and customer relations,
- Monitoring and enforcement of service quality and performance targets,
- Application and enforcement of tariff policies and rules, and
- Resolution of customer complaints that are not resolved satisfactorily by the service providers.

If the current staffing of the CMU is assessed, from the perspective of these two core functional areas, some of the current staff does not possess the prior training, nor the type and years of experience, in these two areas, that are required to be successful. During the course of this Advisory engagement, two senior members of staff were recruited by the CMU, for finance and legal. Their addition to staff represents a major increase in capacity.

The current staff has the capacity to acquire the needed skills, while experience can only come from performing the assigned duties.

8.8 Definition of Recommended Organizational Structure and Summary Position Descriptions for the CMU

The organizational structure being proposed by the Advisory Team, parallels this idea of two core functional areas. A proposed Organizational Structure has been prepared and included in the section. The senior management team, within this Organizational Structure, is as follows:

- Executive Director
- Director of Economic and Regulatory Research
- Director of Technical Research and Evaluation

- Director of Contract Management

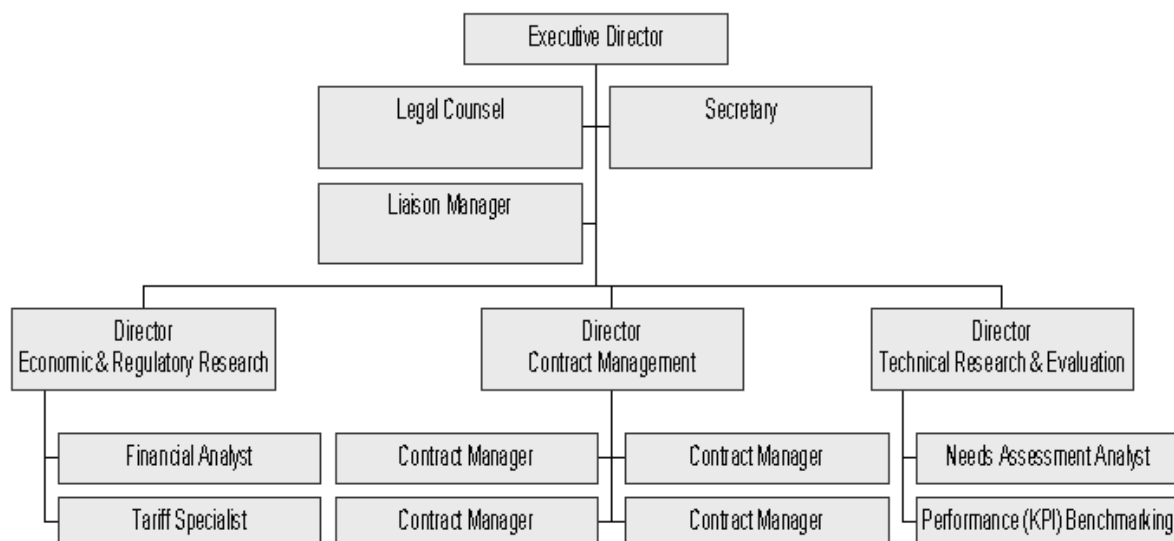
The central thrust of the CMU is to collaborate with Council (Portfolio Committee) in forming policy for a given service (sector), capturing that policy in the form of a “scope of services” in the SDA, and then monitoring that performance against the SDA.

The collaboration process engages both the Contract Managers, who deals with the current situation and the practicalities of change, as well as the Research Sections, who help identify and analyse the other options and impacts.

The process of capturing the desired policy outcome in an SDA is a procurement process. The Contract Manager is central to this effort and works closely with the Legal Services Section of the Corporate Services Unit to prepare the SDA. In this situation, the Legal Services Section is responsible for the contractual terms and conditions, while the Contract Manager is responsible for the development of the scope of services, standards of performance, key performance indicators, and methods for monitoring performance.

During the SDA implementation phase, the Contract Manager monitors the performance of the UAC under the SDA. Concurrently, the Research Sections are engaging independent services to measure satisfaction of the public with the services delivered.

Suggested Organizational Structure of CMU



Summary position descriptions of the CMU's proposed senior management team are as follows:

- **Executive Director**

Directs the overall performance of the CMU and sets priorities/allocates resources to perform the mission of the CMU. Accountable to the City Manager, and reports to those Portfolio Committees having responsibility for UAC's. Interacts directly with the Portfolio Committee, Executive Mayor and the City Manager in addressing both the policy development role, as well as the policy implementation role, in the delivery of public services by the UAC's.

- **Director of Economic and Regulatory Research**

Provides direct financial and economic analysis support to the Contract Manager, in the SDA negotiation process, as well as undertakes research and policy development in the areas of tariff and fee determination, and willingness-to-pay. In addition, this position coordinates with all other regulators in South Africa, that impact on the performance of the UAC's to insure that the UAC's and the SDA's comply with current regulatory practices in South Africa.

- **Director of Technical Research and Evaluation**

Provides direct technical management support to the Contract Manager, in the SDA negotiation process, as well as undertakes research and policy development in the areas of best practice, benchmarking, and KPI's. In addition, this position contributes to the development of policy by undertaking needs assessments in the each of the public service areas, and recommending policy options to address needs that are not being met.

- **Director of Contract Management**

Provides the overall direction to the procurement and negotiation process as it relates to capturing the policy objectives in the SDA's. Ensures that contract management (performance monitoring) is conducted on a standardized and documented way, and that the conduct and professionalism of the Contract Managers is of the highest standards to protect the interests of the Council.

The following is a brief description of the functional activities that occur under each of the proposed Director positions. No attempt has been made to quantify the actual number of staff needed in each of the functional areas. This can be considered in a later phase of this implementation strategy development process.

8.8.1 Economic and Regulatory Research

This section of the CMU will staff specialists with expertise in the areas of financial analysis, financial performance measures, financial/economics research, tariff policy, tariff determination and negotiation, and economic regulatory practices.

8.8.2 Technical Research and Evaluation

This section of the CMU will staff specialists with expertise in the areas of public services needs assessment, key performance indicators and reporting, technical performance measures and benchmarks, technical best practice, operational assessment, and asset condition evaluation.

8.8.3 Contract Management

This section of the CMU will staff specialists with expertise in the areas of scope of services development and negotiation, procurement process management, contractor liaison, compliance monitoring and documentation, and conflict/dispute resolution.

8.9 Funding Options to Sustain the Activities of the CMU

A very popular theme in public administration, today, is the idea of cost-centre based accounting, with full recovery of costs from the services delivered. This idea, taken to its limit, in the case of the CMU, would imply that the CMU would charge each of the UAC's some calculated amount, to offset the cost of the CMU. In this way, it would put the cost of the CMU back on the users of the public service, rather than taking it out of City's general revenues.

This is a very plausible approach to financing the cost of the CMU, and is a routine way that independent regulators finance their operations in many countries. For a number of the UAC's, who actually never cover their costs out of tariffs or fees from the served public, it results in an increase in the subsidy provided by the City, and therefore it comes out of general revenues. Yet, it is a good discipline, from an accounting standpoint.

PropCom currently uses a similar approach in financing its operations as a UAC.

9. Recommended Actions to Strengthen and Empower the CMU in the Performance of its Role and Responsibility

9.1 Review and Finalize Report

Issue the Draft Report to all parties affected by the role of the CMU, and solicit comments for the preparation of the Final Report.

9.2 Reach Consensus on Redefined Role for the CMU

Conduct a workshop/series of meetings to discuss the recommendations of the Advisory Team's recommendations, in this Report, and reach a consensus on the role of the CMU going forward.

9.3 Agree on Organization Structure/Staffing Plan

Issue the Final Report to all parties affected by the role of the CMU, and conduct a workshop to discuss the organizational structure/staffing plan, as well as the interfaces and procedures of the CMU going forward.

9.4 Review Compensation Structure for Key Staff

Conduct a compensation analysis for the positions and skills defined in the Organization Structure/Staffing Plan, and establish pay ranges for each position.

9.5 Transfer Shareholder Responsibility to Finance Unit

Work with Finance Unit to define and transfer all shareholder functions related to the UAC's to the Finance Unit.

9.6 Conduct Discussions and Reach Consensus with Legal Services Section of Corporate Services Unit on Way Forward

Work with Legal Services Section of the Corporate Services Unit to define the legal services needs of the CMU and reach consensus as to how and when the Legal Services Section will be a position to assume its role in support of the CMU.

9.7 Define Role and Relationship between CMU and Council Portfolio Committee

Conduct a workshop with the Portfolio Committees directly supported by the CMU to clearly define the new role of the CMU, and to reach an objective consensus as to the relationship between the CMU and each of the Portfolio Committees. One emphasis of the workshop will be to develop a clear understanding, on the part of the Portfolio Committee Members, of the proper point of interface between the Portfolio Committee and a UAC.

9.8 Define Role of Regional Directors in Monitoring Service Delivery and Relationship with CMU

Based on decisions made by Portfolio Committees on the new role, work with the Regional Directors to come to a consensus as to their role in implementing it. Regional Directors are best able to monitor service delivery to the public in their regions, and work together to establish procedures that the Regional Directors will follow when they receive a complaint or concern from the public in their region concerning municipal services.

9.9 Review, Revise and Approve Procedures and Guidelines Manual

Once the various actions described above have been adequately addressed, and a consensus has been reached on each, the CMU should make revisions to the various procedures and guidelines manuals that have been prepared by the various consultants retained by the CMU.

10 Time Schedule to Transform CMU Based on Recommended Actions

(This section will be prepared, once the CMU has received feedback from the Mayor Committee relative to the desired direction of the CMU, based on the inputs from the Advisory Team and other advisors to the CMU and the Mayoral Committee.)